

ABC Privatization and State Revenue



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ABC Revenue Objectives in Making the Change to Privatization

There are three basic types of ABC revenue and each has a different objective within the privatization effort.

General Fund Revenue

The objective is to minimize the impact of privatization on the amount of revenue currently collected in the general fund.

Recovery of Enforcement and Regulatory Cost

The objective is to fully recover costs from the regulated community and to provide for increased enforcement after privatization.

Sale of the Right or Privilege to Buy/Sell Liquor (Wholesale and Retail) in Virginia and Sale of Surplus Assets Currently Held by ABC.

The objective is to maximize this revenue stream and use it for transportation needs.

Maintaining General Fund Revenue After Privatization - Current Revenue

- The General Fund will receive (budgeted) \$324.2 million in FY2011 from alcohol-related taxes and ABC profits. This revenue comes from:
 - An excise tax imposed at the rate of 20% on the sales price of distilled spirits is expected to generate \$111.4 million in fiscal year 2011,
 - An excise tax imposed on beer at a rate of \$7.95 per barrel is expected to generate \$43.4 million in fiscal year 2011,
 - A wine liter tax imposed on wine at a rate of \$0.40 per liter sold is expected to generate \$29.1 million in fiscal year 2011,
 - A retail sales tax imposed at 5% of the sale price on ABC products sold at state stores is expected to generate \$25.6 million in fiscal year 2011, and
 - ABC profits and cost savings transferred to the general fund that are expected to be \$114.7 million in fiscal year 2011. (ABC currently places a mark-up tax of up to 79% on distilled spirits depending on container size and type of product. For 750ml and liter bottles, the mark-up is 69%).

Maintaining General Fund Revenue After Privatization – Proposed Revenue

- After privatization, the ABC markup and excise taxes charged at state stores will no longer be collected (-\$226.1 million).
- To replace these revenues, the following is proposed:
 - An excise tax on distilled spirits at a rate of \$17.50 per gallon (applied at the wholesale level) would be imposed generating approximately \$175.7 million per year with \$165.7 million going to the general fund, and \$10.0 million going to the enforcement and regulatory functions.
 - An optional convenience fee at a rate of 2.5% (applied at the retail level) for on-premise sales would be imposed generating approximately \$19.4 million a year for the general fund. On-premise establishments will benefit from wholesale prices and delivery.

Maintaining General Fund Revenue After Privatization – Proposed Revenue

- There would be no change to the structure of the beer excise tax, the wine excise tax or the retail sales and use tax.
- However, increased distilled spirit and wine sales (due to convenience and repatriation of lost sales) are anticipated to generate an additional \$700,000 wine taxes and an additional \$14.0 million in retail sales taxes for the general fund. Virginia will still be below the national average for per capita sales (by volume).
- Finally, business income taxes are expected to increase about \$5.8 million a year for the general fund as private firms take over the wholesale and retail distribution network for distilled spirits.

Recovering Regulatory Costs and Enhancing Enforcement – Current System

- The cost of ABC operations (including enforcement, hearings, stores and warehouse operations, and other functions, but excluding the cost of merchandise sold) totaled \$138.7 million in fiscal year 2010 as follows:

	<u>\$ Millions</u>
Stores and Warehouse Operations	\$ 96.1
Technology Costs	14.7
Enforcement Costs	13.9
Other Expenses	<u>14.0</u>
Total	\$138.7

- Part of this expense, \$13.4 million, is recovered from fees for licenses, applications, analysis of bottle labels, etc. and from fines imposed by the ABC Board.
- The larger part, or remaining \$125.3 million, is paid for out of ABC sales revenue.

Recovering Regulatory Costs and Enhancing Enforcement – Proposed System

- After privatization, the regulatory and enforcement costs for ABC are estimated to be \$31.9 million a year including the additional costs of enhanced enforcement as follows:

	<u>\$ Millions</u>
Stores and Warehouse Operations	\$ 0.0
Technology Costs	6.9
Existing Enforcement Costs	13.9
Additional 22 Enforcement Officers (+25%)	2.4
Other Expenses (e.g., hearings, appeals, office space, etc.)	<u>8.7</u>
Total	\$ 31.9

Recovering Regulatory Costs and Enhancing Enforcement – Proposed System

- The regulatory and enforcement functions would be fully paid for by collecting an estimated \$31.9 million from the regulated community using the following:
 - An estimated \$10.0 million per year for enforcement and regulation from the excise (gallonage) tax on distilled spirits.
 - An annual wholesale license charge assessed at 1% of gross receipts on distilled spirits generating \$7.1 million per year for enforcement and regulation, and
 - A new 3-tiered annual fee structure (\$500, \$1,000, and \$2,000) for the 3 different levels of retail operations generating \$1.4 million per year for enforcement and regulation, and
 - The continuation of \$13.4 million in existing fees per year from on-premise business, application fees, other charges, and fines currently assessed by ABC.

Providing Upfront Revenue for Transportation – Sale of Assets

- A significant amount of revenue could be collected from 3 major sources:
 - Auction of retail licenses to highest bidders,
 - Sale of wholesale licenses, and
 - Sale of ABC warehouse and state-owned retail outlets (the state owns 19 of 332 stores).
- This one-time revenue would be in addition to ongoing revenue sources.
- It would provide a significant contribution (windfall) for transportation needs.

Added Benefit of Increased Local Revenue

- Although local taxation is not a part of the proposed revenue structure, localities will benefit from its implementation.
- Current ABC retail/warehouse operations do not directly pay local taxes. (It is assumed that ABC stores pay real property taxes through their rent or lease agreements since most store space is currently leased).
- Consistent with privatization assumptions, local governments statewide would collect an additional \$4.3 million in local option sales taxes, business license (BPOL) taxes, and local meals taxes.
- This additional revenue could be used for local ABC enforcement enhancement or other local needs as determined at the local government level.

Summary and Conclusions

- The privatization proposal for ABC meets the individual objectives for the various types of revenue.
 - 94 percent of general fund revenue is maintained,
 - Affected private entities pay for enforcement and regulation,
 - Significant upfront resources for transportation will come from the sale of license and current assets held by ABC, and
 - As an added benefit, localities collect more revenue for enhanced enforcement or other local needs.

Summary and Conclusions

- While the points of revenue collection will change as the state moves from a single government controlled wholesaler and retailer – there is no tax increase.
- Going forward, taxes and fees are evenly distributed over all of the participants in the liquor sales and distribution business (wholesalers, retail stores, restaurants/hotels, consumers).
- Restaurants and hotels will have the option to pay a convenience fee to receive the benefit of wholesale discount prices and delivery.
- Enforcement will be strengthened with the addition of 22 new ABC enforcement agent positions (25% increase).